

Message Text

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15

ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CIAE-00 COME-00 EB-07 FRB-03

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CEA-01 DODE-00 PM-04 H-02 L-03 PA-01 PRS-01 IO-11

AGR-05 /107 W

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FM AMEMBASSY BONN

TO SECSTATE WASHDC 6620

INFO AMEMBASSY LONDON

AMEMBASSY PARIS

AMEMBASSY ROME

USMISSION EC BRUSSELS

USMISSION OECD PARIS

AMCONSUL BREMEN

AMCONSUL DUSSELDORF

AMCONSUL FRANKFURT

AMCONSUL HAMBURG

AMCONSUL MUNICH

AMCONSUL STUTTGART

USMISSION USBERLIN

CINC USAFE RAMSTEIN

CINC USAREUR HEIDELBERG

CINC EUR VAIHINGEN

C O N F I D E N T I A L SECTION 01 OF 02 BONN 02939

DEPARTMENT PASS TREASURY AND FEDERAL RESERVE

E.O. 11652: GDS

TAGS: EFIN, ECON, GW

SUBJECT: GERMAN EXPERTS' IMPRESSIONS ON THE

ECONOMIC OUTLOOK : OUTRIGHT OPTIMISM

VERSUS PERSISTENT UNCERTAINTY

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1. SUMMARY. CONVERSATIONS WITH TWO LEADING ECONOMISTS AND AN ECONOMICS MINISTRY OFFICIAL ON THE FUTURE COURSE OF GERMANY'S ECONOMY ELICITED SOMEWHAT VARYING OPINIONS ON HOW GOOD THINGS REALLY LOOK. HORST SEIDLER, WHO HEADS THE BERLIN ECONOMIC RESEARCH INSTITUTE'S (DIW) DOMESTIC ANALYSIS DEPARTMENT, WAS MOST OPTIMISTIC. ON THE OTHER HAND, ARMIN GUTOWSKI, ONE OF THE "FIVE WISEMEN" ON THE COUNCIL OF ECONOMIC EXPERTS, WAS MORE CAUTIOUS ON THE OUTLOOK AND THOUGHT THAT FURTHER EXPANSIONARY PROGRAMS SHOULD BE READIED ON A CONTINGENCY BASIS IN THE EVENT THE UPTURN STALLS. AN ECONOMICS MINISTRY OFFICIAL CONFIDED SIMILAR RESERVATIONS AND THOUGHT THAT THE LEADERSHIP WAS TOO COMPLACENT IN VIEW OF THE POTENTIAL FUTURE DANGERS. END SUMMARY.

2. SEIDLER, WHOSE MOST RECENTLY PUBLISHED FORECAST IS FOR 5 PERCENT REAL GNP GROWTH IN 1976, SAID HE WAS EXTREMELY CONFIDENT ON THE SOLIDITY OF THE UPTURN. IN FACT, HE FELT THAT ON THE BASIS OF HIS READING OF THE INDICATORS 6 PERCENT GROWTH WAS MORE PROBABLE, BUT THAT EVERYONE IS STILL TOO AFRAID TO COME RIGHT OUT AND SAY SO. FIRST QUARTER 1976 GNP SHOULD BE CLEARLY HIGHER THAN 1975'S FOURTH QUARTER HE MAINTAINED. UNEMPLOYMENT (NON-ADJUSTED) IS SEEN AS GRADUALLY DROPPING AS THE YEAR PROGRESSES, WITH THE FOURTH QUARTER 1976 AVERAGE BEING 740,000 AND THE AVERAGE FOR THE YEAR RUNNING 975,000. FURTHER GOVERNMENTAL EXPANSIONARY MEASURES ARE THEREFORE DEFINITELY NOT TO BE CONSIDERED, HE ASSERTED. HAVING AT HIS DISPOSAL AN IMPRESSIVE STAFF AND DATA PROCESSING CAPABILITY, TECHNICIAN SEIDLER'S OPTIMISM, WHICH EVEN EXCEEDS THAT OF THE GOVERNMENT, IS NOT TO BE DISCOUNTED.

3. GUTOWSKI THOUGHT THAT WHILE THE 4 TO 5 PERCENT GROWTH THAT THE GOVERNMENT AND COUNCIL FORECAST WILL LIKELY BE REACHED, GIVEN THE ANGLE OF THE UPTURN UNDERWAY, HE WAS LESS SANGUINE ABOUT THE DURABILITY OF IT ALL AND THAT LABOR MARKET DEVELOPMENTS WILL BE CONFIDENTIAL

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VERY FAVORABLE. HE SAID THAT HE HAD CONSIDERED SUBMITTING A DISSENTING OPINION TO BE APPENDED TO THE COUNCIL OF ECONOMIC EXPERTS ANNUAL ECONOMIC REPORT THAT WOULD BETTER REFLECT HIS LACK OF CONFIDENCE AND LESS OPTIMISTIC VIEW, BUT THAT HE HAD BEEN DISSUADED FROM DOING SO. HE FELT THAT THE MORE QUALIFIED LANGUAGE THAT WAS FINALLY INTRODUCED AS A COMPROMISE MEASURE WAS SUFFICIENTLY, IF NOT FULLY, SATISFYING

ON THIS POINT.

4. GUTOWSKI THOUGHT THAT THE UNCERTAINTIES AS TO THE DURATION OF THE GERMAN UPTURN DERIVED FROM THE EXTERNAL SECTOR. DOUBT WAS EXPRESSED AS TO HOW STRONG DEMAND FOR GERMAN EXPORTS WOULD BE -- ESPECIALLY IN THE CASE OF THE UK AND ITALY. IN THE ABSENCE OF A SOLID GROWTH IN EXPORTS, HE COULD SEE THE NASCENT RECOVERY QUICKLY PETERING OUT. (NOTE: EXPORT ORDERS HAVE BEEN ON THE DECLINE SINCE OCTOBER.) THIS BEING THE CASE, HE SAID HE THOUGHT THAT THE GOVERNMENT SHOULD BE CONTEMPLATING THE POSSIBLE NEED FOR FURTHER EXPANSIONARY MEASURES. THESE SHOULD BE WITHIN THE ANNOUNCED MONETARY GROWTH GUIDELINES AND CONSIST OF

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INFO OCT-01 ISO-00 AID-05 CIAE-00 COME-00 EB-07 FRB-03

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CIEP-01 LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-04

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FM AMEMBASSY BONN

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INFO AMEMBASSY LONDON

AMEMBASSY PARIS

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USMISSION EC BRUSSELS

USMISSION OECD PARIS

AMCONSUL BREMEN

AMCONSUL DUSSELDORF

AMCONSUL FRANKFURT

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C O N F I D E N T I A L SECTION 02 OF 02 BONN 02939

EXPANDED GOVERNMENTAL SPENDING. A DM 10 BILLION PROGRAM MAGNITUDE WAS MENTIONED. SCHOOL AND HOSPITAL CONSTRUCTION BY THE COMMUNITIES WITH FEDERAL HELP WERE EXAMPLES HE CITED. ADDITIONAL INVESTMENT OUTLAYS BY THE BUNDESBAHN, BUNDESPOST AND MILITARY WERE, IN CONFIDENTIAL

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HIS VIEW, ALSO AREAS WHERE SUCH EXPANSIONARY SPENDING MIGHT BE DIRECTED.

5. GUTOWSKI'S RECOMMENDATION TO PREPARE CONCRETE PROGRAMS ON A CONTINGENCY BASIS, HE LAMENTED, HOWEVER, WAS NOT APPARENTLY HAVING ANY SUCCESS DUE (AT LEAST IN PART) TO THE OPPOSITION OF FINANCE MINISTER APEL AND ECONOMICS MINISTRY OFFICIALS SCHLECT AND TIETMEYER. IT IS THEIR FEAR OF THE NEGATIVE PSYCHOLOGICAL IMPACT OF SUCH PREPARATORY STEPS THAT CAUSES THEM TO HESITATE, SAID GUTOWSKI. EXPECTATIONS FOR FUTURE ECONOMIC PERFORMANCE WOULD BE LOWERED IF WORD GOT OUT THAT ANYTHING LESS THAN AN ASSURED ROSY PICTURE WAS ANTICIPATED BY THE GOVERNMENT. THE SELF-FULFILLING PROPHECY EFFECT WOULD CHANGE FROM THE POSITIVE TO THE NEGATIVE. AS A RESULT, ANY SUCH CONTINGENCY PLANNING MUST BE KEPT IN THE UTMOST SECRECY, IF IT IS TO BE DONE AT ALL. EXTREMELY HEAVY RELIANCE WAS BEING PLACED ON THE USE OF PSYCHOLOGICAL MANIPULATIONS RATHER THAN MACROECONOMIC TINKERING BY THE FRG ECONOMIC LEADERSHIP TO SPUR THE ECONOMY ON, HE OBSERVED.

6. THIS BEING AN ELECTION YEAR, THE UNEMPLOYMENT PROBLEM IS CRUCIAL, OPINED GUTOWSKI. THE PERCEPTION OF AN IMPROVED LABOR MARKET PICTURE IS CRITICAL TO THE SPD/FDP COALITION'S SUCCESS. HOWEVER, HE CONFESSED THAT THE COUNCIL'S ASSUMPTION OF A 4 PERCENT PRODUCTIVITY RISE IN 1976 WAS TOO LOW; RATHER, IT COULD REACH 6 PERCENT. THE RESULTANT IMPLICATION OF THIS IS THAT THE COUNCIL'S 1976 FORECAST OF A DECLINE IN EMPLOYMENT OF 275,000 MAY BE TOO LOW, AS MAY ITS 1,000,000 AVERAGE UNEMPLOYED PROGNOSTICATION FOR THIS

YEAR. DR. GUTOWSKI THOUGHT IT ALREADY TOO LATE TO DO ANYTHING AT THIS STAGE IN ORDER TO AFFECT LABOR MARKET CONDITIONS IN THE SEPTEMBER/OCTOBER ELECTORAL PERIOD. EVEN SO, IF IN MARCH THE ECONOMIC INDICATORS PORTRAY THE SAME LACK OF VITALITY OBSERVED IN THE DECEMBER DATA, HE COULD SEE THE GOVERNMENT MOVING ITSELF TO ACT IN AN EXPANSIONARY MANNER.

7. AN ECONOMICS MINISTRY OFFICE DIRECTOR WORKING FOR
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TIETMEYER TOLD US THAT THERE SEEMED TO BE THE (MISTAKEN) PERVADING IDEA IN THE UPPER REACHES OF THE FRG HIERARCHY THAT THE ECONOMIC PROBLEMS WILL SOMEHOW SOLVE THEMSELVES. HE OPINED THAT THE FRG LEADERSHIP WAS NOT FULLY COGNIZANT OF THE POTENTIAL DANGERS THAT LIE AHEAD IN TERMS OF BUSINESS CYCLE AND LABOR MARKET DEVELOPMENTS. THE WEAKNESS OF THE FOREIGN MARKET AND THE HEAVY GERMAN DEPENDENCE ON EXPORTS WERE HIGHLIGHTED. HE FORESAW NO FURTHER IMPROVEMENT ON THE INFLATION FRONT IN 1976 AND SAID THAT ONE MUST REGARD WITH SKEPTICISM HIS MINISTRY'S FORECAST OF ONE MILLION AVERAGE UNEMPLOYED IN 1976. ACCORDING TO OUR CONTACT, THE PRODUCTIVITY INCREASE OF 4.5 PERCENT INHERENT IN THIS FIGURE IS BEING DISPUTED BY LABOR MINISTER ARENDT WHO MAINTAINS 5.5 PERCENT IS MORE LIKELY AND THEREFORE SO ALSO THE LIKELIHOOD OF HIGHER UNEMPLOYMENT. (WHETHER THIS IS PART OF A BROADER ARGUMENT BY ARENDT IN THE CABINET FOR A MORE EXPANSIONARY POLICY WAS NOT SPECIFIED.) THE ECONOMICS MINISTRY SAW 1977 AS BEING A YEAR OF SERIOUS ECONOMIC AND FINANCIAL PROBLEMS. WHILE THE TVA INCREASE PROPOSAL WAS TEMPORARILY KILLED, GIVEN THE OPPOSITION-CONTROLLED BUNDESRAT, HE FORESAW AN UNAVOIDABLE INCREASE TAKING PLACE BY MID-1977 DUE TO THE FISCAL REALITIES THAT WOULD BY THAT TIME BE RECOGNIZED BY ALL PARTIES (THE LAENDER WILL NEED THEIR SHARE OF THE INCREASED TAKE) IN THE POST-ELECTORAL PERIOD. STEPS WILL ALSO HAVE TO BE TAKEN AT THAT TIME TO CUT BACK ON THE OTHERWISE BUILT-IN INCREASE IN GOVERNMENTAL SOCIAL WELFARE OUTLAYS. THIS WOULD BE DONE NO MATTER WHO WINS THE ELECTION, AND HE THOUGHT THE SPD/FDP COALITION BY NO MEANS A SURE THING ("...THEY ARE IN TROUBLE...").
HILLENBRAND

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